

Refining IFRS

IFRS financial reporting issues in the mining and metals sector

Revenue from Contracts with Customers - impact on the mining sector

February 2011



Our Refining IFRS series examines the complex, but unique, issues faced by mining and metals companies in applying IFRS. These issues are considered in the context of recent and current developments in the global mining and metals marketplace. This issue provides a high-level overview of the potential implications of the new revenue recognition proposals on the mining industry.

Introduction

We issued a publication entitled *Revenue from Contracts with Customers: The road to convergence: what the revenue proposals mean in practice*¹ summarising the revenue recognition model proposed in the joint Exposure Draft (ED) of the International Accounting Standards Board (IASB) and the US Financial Accounting Standards Board (FASB) (together, the Boards). We also highlighted some issues for companies to consider in evaluating the merits of the ED and some of the expected changes to current IFRS.

In this issue of *Refining IFRS* we look at some of the more significant implications that the proposed revenue recognition model may have for the mining sector.

The issues discussed here are intended to both provoke thought and assist companies in formulating ongoing feedback to the Boards that can help in the development of a high-quality final standard. Nevertheless, these discussions do not represent final or formal views and additional issues may be identified, as elements of the ED are subject to change based on further deliberation by the Boards before a final standard is issued.

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¹ Available on ey.com/ifrs

Scope

Definition of revenue and a customer

Revenue is currently defined in IFRS as:

“Income arising in the course of an entity’s ordinary activities.”

This definition has been carried forward unchanged in the ED. The Boards noted in the Basis for Conclusions to the ED that they would not revisit the definition of revenue as part of this project, but instead would do this as part of their joint Conceptual Framework project.

The proposed revenue recognition guidance in the ED then only applies to revenue from contracts with customers. That is, it only deals with a subset of an entity’s potential revenue generating activities. The ED defines a customer as:

“... a party that has contracted with an entity to obtain goods or services that are an output of the entity’s ordinary activities.”

Neither current IFRS nor the ED defines “ordinary activities”. The Boards indicated in the Basis for Conclusions to the ED that they were not going to clarify the meaning of “ordinary activities” because that notion was derived from existing revenue definitions, which as noted, were not being revisited as part of this project.

How we see it

There are many complex contracts in the mining industry and diversity currently exists in how these are accounted for. By not revisiting the definitions of revenue or ordinary activities, while proposing a model that only deals with a subset of an entity’s total revenue generating activities, there is a risk of creating further uncertainty as to what constitutes an entity’s ordinary activities and, hence, represents total revenue.

Determining who is a customer will require an assessment of the individual facts and circumstances. Without specific guidance as to what are considered an entity’s ordinary activities may lead/add to divergent interpretations.

Generally, if a contract was not previously considered to be a customer contract, we do not believe this ED will change this. Having said this, in some cases this may not be clear. Therefore some contracts (e.g., production sharing contracts, royalty agreements) may need to be evaluated to determine if they represent customer contracts.

It is our understanding that should a contract or arrangement not fall within the scope of this ED, it does not necessarily preclude the potential inflows arising from such contracts from being described as part of total revenue (albeit from non-customers).

Other scope exemptions

The proposed revenue recognition guidance states that if a contract is partially within the scope of another standard, then the provisions of that other standard (e.g., accounting for an embedded lease or an embedded derivative) are applied to that specific section of the contract. As such, the scope of the proposed revenue recognition guidance excludes leases, among other contracts.

How we see it

Although the criteria for determining what is or is not a lease will not change under the proposed leasing ED, this assessment will take on increased importance.

The current accounting for operating leases and service contracts is often similar. Therefore, determining that a service arrangement contains an operating lease generally does not result in significantly different accounting. Consequently, it is possible that not all embedded leases have been identified, extracted and/or accounted for as such.

Given the proposed accounting for operating leases in the new lease model will be completely different, this assessment will have significantly different accounting implications where service contracts are considered to contain embedded leases and therefore entities may need to evaluate current and future contracts more closely.

Sale of gold bullion

When mining entities sell gold bullion, there is a period of time (usually a matter of days) between the bullion leaving the mine site with the security shipper and the gold being credited to the metal account of the customer. In the intervening period, the gold bullion is sent to the refinery, refined, out turned, credited to the entity's metal account and, finally, transferred to the customer's metal account.

Current practice

It is common practice for revenue to be recognised on such gold bullion sales when the bullion leaves the mine site with the security shipper.

Potential impact of new proposals

Under the proposed model, revenue is recognised only when an identified performance obligation is satisfied by transferring control of the promised good to the customer. Control is defined in the ED as:

"... an entity's ability to direct the use of, and receive the benefit from, a good."

Control would also include the ability to prevent other entities from directing the use of, and receiving the benefit from, the good. The transfer of control to the customer also represents the transfer of all rights with regards to the good.

In relation to gold bullion sales, at the point the gold bullion leaves the mine site:

- ▶ The customer does not have physical control of the product.
- ▶ Title generally has not passed to customer.
- ▶ There is usually no unconditional obligation for the customer to pay.
- ▶ The customer would not have the ability to direct the use of, nor receive the benefit from, the gold bullion.

It is likely that these criteria will usually only be satisfied once the gold is actually credited to the customer's metal account.

How we see it

Given it is unlikely that control will be deemed to pass to the customer prior to the gold bullion being credited to the customer's metal account, the timing of current revenue recognition practices of some gold bullion producers is likely to be impacted by this proposed new model.

Provisionally priced sales

Sales contracts for certain commodities (e.g., copper) often include provisional pricing at the time of shipment of the metal concentrate, with final pricing based on the average market price for a particular future period. This type of arrangement is particularly common when an entity produces a mineral concentrate that is sold to a smelter or refiner, which produces the fully refined metal that is then sold into the market.

The final sales price is often:

- ▶ Based on the average market prices during a subsequent period (the 'quotational period')
 - ▶ The price on a fixed date after delivery
- Or
- ▶ The amount subsequently realised by the smelter or refiner, net of tolling charges

Current practice

Price adjustment features contained in non-cancellable contracts that are based on quoted market prices for a date subsequent to the date of shipment or delivery (e.g., the spot price three weeks after shipment, or the average spot price for the month of shipment), are generally considered to be embedded derivatives that require separation under IAS 39 *Financial Instruments: Recognition and Measurement*. This is because the forward price at which the contract is to be settled is considered not to be closely related to the spot price.

If the contract is cancellable without penalty before delivery, the price adjustment feature does not meet the definition of a derivative at the point of entering the contract because there is no contractual obligation until delivery takes place. If the contract is not cancellable, there will be a contractual obligation when the contract is first entered into. However, the embedded derivative would be considered to be closely related to the host commodity contract and, as such, does not need to be recorded separately until delivery.

When the embedded derivative is separated from the host contract, the host contract will normally meet the revenue recognition criteria - in particular, the requirement that revenue can be measured reliably - at the date that the mineral concentrate is delivered.

Any changes in the fair value of the embedded derivative should be recognised in profit or loss for the period. In relation to any subsequent fair value movements, IAS 39 does not specify exactly where these should be presented in profit or loss. Consequently, there is currently divergent practice as to where these fair value gains or losses are presented in profit or loss. Some industry participants present these movements as adjustments to revenue, while others present these as part of derivative/other gains and losses.

Potential impact of new proposals

The scoping section of the ED states that if a contract is partially within scope of this ED and partially in scope of another IFRS, if the other IFRS specifies how to separate and/or initially measure any parts of the contract, an entity shall first apply those separation and/or measurement requirements.

Given these provisional pricing features are generally considered to represent embedded derivatives within the scope of IAS 39, entities would be required to continue to separate these² out at the point of delivery (which is when they come into existence) and recognise and measure them in accordance with those standards. Hence, they would not be within the scope of the revenue recognition ED.

How we see it

The ED makes it clear that these provisional pricing features should continue to be accounted for under IAS 39 and therefore they will be outside the scope of the revenue recognition ED.

However, without further clarification as to what constitutes total revenue from ordinary activities, while proposing a model that only deals with a subset of total revenue, means it remains unclear whether such movements could continue to be adjusted against revenue.

Production sharing contracts/ arrangements (PSCs)

While PSCs are most common in the oil and gas industry, similar arrangements do exist in the mining industry and can be referred to as PSCs or Contracts of Work (for simplicity, herein referred to as PSCs).

A PSC is a contract between some form of national government entity of a host country and a contracting enterprise (the mining company) to carry out minerals exploration, development and production activities, or any combination of the three, in accordance with the specific terms of the contract. The contractor will generally be responsible for extracting the government entity's share of production from the mine. The mining entity is typically responsible for 100% of exploration costs and some or all of development and production costs.

Current practice

Currently, there is no specific guidance within IFRS governing the accounting for PSCs. These contracts are generally considered to be more akin to working interest relationships than pure services contracts. This is because the mining company is assuming risks associated with performing mining activities and is receiving a share of future production as specified in the contract.

Under current IFRS, revenue is recognised once production commences and upon sale of the mining company's share of the extracted minerals to third parties as opposed to being recognised as a fee for services rendered pre-production.

Potential impact of new proposals

In determining whether a contract between the government entity and a mining company is within the scope of the ED, an entity must look to the definition of a customer and what constitutes "ordinary activities", as discussed above.

² NOTE: This potential implications arising from IFRS 9 and the change in accounting for financial instruments with embedded derivatives, have not been discussed in this publication.

How we see it

As the Boards appear to have relied on current definitions of revenue and “ordinary activities”, we believe the relationship between a mining company and the government entity is likely to continue not to represent a customer relationship relating to the provision of services. Therefore, such contracts could be outside the scope of this ED.

Having said this, the terms and conditions of contracts with governments continue to evolve, particularly given the percentage of the world’s mineral reserves that are owned by governments. As such, the facts and circumstances of all arrangements should be carefully assessed to determine whether the relationship between the two parties changes and potentially becomes a supplier-customer relationship and, hence, falls within scope.

Take-or-pay contracts

A take-or-pay contract is an agreement between a buyer and seller in which the buyer will still pay a specified minimum amount even if the product or service is not provided.

While take-or-pay contracts are most commonly used in the oil and gas industry and usually involve the supply of gas, they are also used in the mining industry, although less frequently, e.g., coal.

Some take-or-pay contracts include a clause that allows a customer to ‘make-up’ the missing output/capacity at a later date. The ability to make up the unused volumes at a later date means that consideration has been received in advance by the producer for a product that has not yet been delivered.

Current practice

Under current IFRS, revenue is recognised as follows:

- a) **Volumes taken:** revenue is recognised when the volumes of the product concerned, e.g., coal, are actually delivered and they are measured at the applicable price at that time, e.g., market price or contract price (as specified in the contract);

b) Volumes not taken but paid for:

- i) Where the customer is not entitled to future recovery of the product paid for, but not taken, revenue is recognised when the payment is due from the customer.
- ii) Where the customer is entitled to apply the payments made in relation to unused product to future deliveries, the amount paid by the customer is recognised as deferred revenue, and is recognised as revenue either when the payment is applied to future deliveries or the right to apply the payment to such deliveries expires unused.

Potential impact of new proposals

Some of the key aspects of the proposed new model which will increase the complexity of, and may change the accounting for, take-or-pay contracts are:

- ▶ Determining whether a long-term take-or-pay contract should be segmented into multiple contracts and/or whether separate performance obligations should be identified
- ▶ Determining and allocating the transaction price
- ▶ Accounting for payments received for unused product that can be made up by applying to future volumes

To illustrate these, we will use the following fact pattern:

Coal Company A enters into a 5-year take-or-pay contract for a minimum of 1,000mt of coal per year. The amount paid for each metric tonne is the market price as calculated in accordance with the terms of the contract, e.g., the volume weighted market price 5 days prior to delivery or for minimum volumes not taken, 5 days prior to the end of that contract year.

In Year 1, Company A delivers 900mt of coal. The purchaser is required to pay for the full 1,000mt, but it is permitted to make up the 100mt of coal in a subsequent period. CU7,000 is received by Company A in relation to the 100mt of unused coal.

Identifying the contract and performance obligations

Segmenting the contract

The ED considers the concept of segmenting a contract if certain criteria are met. That is, while there may be only one physical contract, for the purposes of revenue recognition, it may be considered to be multiple contracts.

Segmentation is required where the prices of some goods or services in the contract are independent of other goods and services in the contract.

While we understand that the purpose of segmenting contracts is to effectively “ring fence” the allocation of the transaction price, i.e., subsequent changes in the transaction price attributable to a segment of a contract are only allocated to the performance obligations within that segment, this is not necessarily clear within the current wording of the ED.

Without further clarification, it may be difficult to determine if a take-or-pay contract comprises multiple contracts and/or multiple performance obligations (refer below).

Considering the example above:

- ▶ Is there one contract spanning five years for the delivery of a minimum of 5,000mt of coal?
Or
- ▶ Are there five contracts for the delivery of 1,000mt of coal per year?

Identifying performance obligations

Regardless of the number of contracts that are identified, an entity needs to identify all promised goods or services and then account for each as a separate performance obligation where they are distinct. Our general revenue recognition publication mentioned above explores in more detail what is meant by “distinct”.

One of the potential issues with this requirement is determining the level of granularity needed to identify these performance obligations. Based on the proposed guidance, it may be difficult for entities to identify the performance obligations in transactions including a large number of goods or services delivered over a period of time, e.g., take-or-pay contracts.

Again, considering the example above, some possible performance obligation scenarios may be that there is/are:

- ▶ One performance obligation for the delivery of 5,000mt of coal
- ▶ Five performance obligations for the delivery of 1,000mt of coal per year
Or
- ▶ 5,000 performance obligations for the delivery of 1mt of coal over five years

Determining how a take-or-pay contract should be accounted for will have significantly different implications for revenue recognition. The ED, however, is not necessarily clear as to how this determination should be made.

Determining the transaction price

The transaction price reflects the probability-weighted amount of consideration that an entity expects to receive from the customer in exchange for transferring the goods or services.

Variable consideration

The ED states that, where the transaction price is variable, an entity should only recognise revenue where the transaction price can be reasonably estimated. If an entity lacks the ability to make a reasonable estimate, the transaction price is limited to the amount of consideration that is fixed or that can be reasonably estimated.

Our general revenue recognition publication explores some of the factors to be considered when assessing whether the transaction price can be reasonably estimated. One such factor is the degree to which the consideration is highly susceptible to external factors, such as market volatility.

The other significant change in the ED is the requirement to update the transaction price for subsequent changes and allocate these changes to each of the performance obligations - both those that have been satisfied and those that are still outstanding.

This will increase complexity and, depending upon how this is interpreted, could potentially lead to some very unusual revenue recognition profiles.

The nature of take-or-pay contracts is that they tend to extend over long periods of time and generally the prices are not fixed, instead they are often based upon/derived from market prices. Therefore, estimating the transaction price at contract inception and throughout the contract period may prove to be difficult or may not be possible.

To illustrate this point, consider the fact pattern in the example above - assume there are five performance obligations to deliver 1,000mt of coal per year over five years and that the customer takes the minimum amount each year, in full, at the same time each year, and pays the market prices listed below.

A potential interpretation of the requirements regarding variable consideration based upon market factors, could inappropriately lead to the following revenue recognition profile:

Table 1: Comparison of potential revenue recognition profiles

Year	Quantity mt	Price per mt	Cumulative revenue	Revenue recognised in period		Calculation under new model
				IAS 18	Proposed model	
1	1,000	CU70	70,000	70,000	14,000	$(70,000 / 5)$
2	1,000	CU75	145,000	75,000	44,000	$((145,000 / 5 \times 2) - 14,000^{**})$
3	1,000	CU80	225,000	80,000	77,000	$((225,000 / 5 \times 3) - 58,000^{**})$
4	1,000	CU85	310,000	85,000	113,000	$((310,000 / 5 \times 4) - 135,000^{**})$
5	1,000	CU90	400,000	90,000	152,000	$((400,000 / 5 \times 5) - 248,000^{**})$

** Already recognised in revenue in prior period(s)

For simplicity, the impact of other factors, such as customer credit, has been ignored.

Given the variable nature of the consideration, the transaction price for the whole contract is only considered to be capable of being reasonably estimated progressively as the actual sales occur. Therefore, as each sale occurs, the transaction price needs to be re-estimated and reallocated, which could result in the unusual revenue recognition profile above.

While the example above is over-simplified, it attempts to demonstrate how determining the profile of revenue allocation could be a significant practical issue in accounting for take-or-pay contracts.

How we see it

Based on more recent discussions with IASB staff, we understand this was not the intended outcome for take-or-pay contracts. Instead, it was intended that, in a situation like the example above, where each portion of the transaction price can only be determined for each performance obligation as it occurs i.e., effectively when the coal is actually delivered or not taken by the end of the period, the known transaction price should only be allocated to the related performance obligation as it occurs.

In the above example, in Year 1, CU70,000 would be the known transaction price and would only be allocated to the first performance obligation, i.e., the deliveries made in Year 1. The remaining portion of the transaction price of the contract would not be reasonably estimable. Then in Year 2, CU75,000 would be the next part of the transaction price that is known and it would only be allocated to the Year 2 performance obligations.

While this may have been the intention, it is not clear how the current wording within the ED would enable this outcome to be arrived at. Therefore, this would need to be clarified in the final standard.

Impact of the time value of money

The proposed model requires that the promised consideration in a contract shall be adjusted to reflect the time value of money where the contract includes a material financing component (explicitly or implicitly).

In most instances, the time value of money will not be material. However, the effect may be material where the payment from the customer is received either significantly before or after the transfer of goods or services.

In take-or-pay contracts, where payments received for unused product can be applied to future volumes, the seller has a performance obligation that has not been satisfied for which consideration has been received in advance. This amount represents a contract liability. In determining whether the time value of money is material (which impacts the measurement of the transaction price, and consequently, the contract liability), an entity will need to estimate when such future volumes are expected to be taken.

Such a determination will be made after consideration is given to the terms of the contractual agreement in conjunction with an assessment of the expected customer behaviours. For example, such an assessment may involve considering whether the make-up volumes are:

- ▶ The first volumes taken at the start of the immediately subsequent period
- ▶ The volumes that can be taken only after the minimum has been taken in the immediately subsequent period or some other future period or
- ▶ Amounts that can only be taken at the end of the contract period

If an entity decides that the time value of money is significant, it would need to impute interest on the contract liability. That is, interest expense would need to be recognised over the period and the value of the contract liability would increase. As a result, the final amount of revenue recognised would be higher when the performance obligation is satisfied.

Using the example above, at the end of Year 1 payment of CU7,000 is received for the 100mt of coal not taken and a contract liability of CU7,000 is initially recognised.

Satisfaction of the performance obligation related to the 100mt is expected to occur only after the subsequent period's minimum is met. Company A determines the discount rate on a similar borrowing.

In Year 2 Company A delivers 1,100mt of coal, the last 100mt of which is delivered in the last month of the year.

During Year 2, Company A recognises interest expense of CU642 [CU7,000 x 10% x 11/12] and increases the contract liability by the same amount. Therefore, immediately before the performance obligation is satisfied, the contract liability is CU7,642.

The entity would then recognise revenue of CU7,642 when it transfers the coal to the customer in the last month of the year.

- ▶ IAS 18 does not explicitly address time value of money. It is implicitly incorporated in the requirement to recognise revenue at the fair value of the amount to be received. However, it would appear that the practice of incorporating the impact of the time value of money is divergent.

For additional guidance on accounting for the time value of money, see our aforementioned general revenue recognition publication.

How we see it

The proposed new revenue recognition model could have significant practical implications for the accounting for take-or-pay contracts. Given the variable nature of the consideration to be received under these contracts, there is a concern that the resultant revenue profile would not reflect the commercial understanding of such arrangements. There is, however, still a considerable lack of clarity as to exactly what the actual impact will be. Having said this, it seems, based on the current proposals, that the complexity in accounting for these arrangements would increase significantly.

Royalty income

Entities in the mining industry sometimes sell part of their interests in a field, or a particular stream of resource (e.g., the owner of a copper/gold resource may sell off access to the mineral sands resource). The transaction may involve an upfront payment and/or a requirement for the acquiring entity to pay a royalty amount over a period of time, based upon a fixed dollar amount per volume of product extracted from the area. Alternatively the acquiring entity may pay a net profit interest being a percentage of the net profit (calculated using an agreed formula) generated by the interest sold.

Current practice

Under current IFRS, accounting for revenue from the extraction of minerals is scoped out of IAS 18. Consequently, different treatments to account for such transactions have emerged. Revenue from royalties is recognised on an accruals basis when the right to receive payment is established, in accordance with the substance of the relevant agreement.

In many instances, given that the right to receive the royalty payment is dependent upon future production, these arrangements tend to be treated as executory contracts. Therefore, revenue is only recognised when the related mineral is extracted.

However, in other instances, where the entity is entitled to receive a certain amount of cash regardless of the level of production, it is considered that this establishes a contractual right to receive cash. Therefore, an entity recognises a receivable and the associated revenue when the arrangement is entered into.

Potential impact of new proposals

As outlined above, the ED only deals with contracts with customers. Therefore, as explained above, an entity would need to determine whether counterparty represented a customer to establish whether this ED would apply.

Should these arrangements be considered to be in scope, some of the same difficulties potentially impacting the accounting for take-or-pay contracts (discussed above), may arise. These include identifying what the performance obligations would be, determining the transaction price (which would be more complicated when there is variable consideration that is dependent upon actions by the customer, i.e., the future extraction of minerals), and the requirement to remeasure and reallocate the transaction price when it changed over time.

How we see it

IAS 18 specifically applies to royalty income. The proposed revenue recognition guidance only deals with revenue from contracts with customers. It is unclear whether counterparties in these forms of royalty arrangements would qualify as customers and therefore would fall within scope of the ED.

If they did, similar to the potential implications outlined above for take-or-pay contracts, this proposed new revenue recognition model may be likely to have significant practical implications in accounting for royalty income, including increased complexity, and may lead to revenue recognition profiles that would not reflect commercial reality.

Royalty payments

Mining entities frequently enter into royalty arrangements with owners of mineral rights. Often these are payable upon the extraction and/or sale of mineral ore. The royalty payments may be based on a specified rate per ton, or the entity may be obliged to dispose of all of the relevant production and pay over a specified proportion of the aggregate proceeds of sale, often after deduction of certain extraction costs.

In other arrangements, the royalty holder may have more of a direct interest in the underlying production and may make mineral extraction and sale arrangements independently. This is often seen in some royalty agreements in the US.

The issue, from a revenue recognition perspective, would be whether revenue should be recognised gross or net of these royalty payments.

Current practice

Currently, the accounting treatment for government and other royalties payable is diverse. Sometimes, all invoiced quantities are included in revenue, and royalty payments are charged either as a cost of sales or as a tax. In other cases, they are excluded from both the value of reported revenue and cost of sales/taxes on the basis that the entity has no legal right to the royalty product.

Potential impact of new proposals

While the ED and associated guidance do discuss some of the issues impacting gross vs net presentation, they do not directly address the treatment of royalties.

Having said that, the ED requires revenue to be recognised at the “transaction price” and Appendix A defines the transaction price as:

“... the amount of consideration that an entity received, or expects to receive, from a customer in exchange for transferring goods or services, excluding amounts collected on behalf of third parties (for example, taxes).”

Other than this, there is no additional guidance provided. Consequently, the ED does not clarify whether a royalty is a cost of production/tax, and therefore, revenue should be recognised gross. Nor does the ED disclose whether a royalty is considered a tax collected on behalf of the lessor (which is usually the government, but could be another party) and hence would be excluded from revenue.

How we see it

It is unclear from the revenue recognition ED whether revenue should be recognised gross or net of royalty payments. Without further guidance, divergence is likely to continue.

Inventory exchanges

From time to time, entities in the mining industry may exchange inventory with other entities in the same line of business. This can occur with commodities such as uranium, coal or certain concentrates, where suppliers exchange or swap inventories in various locations to supplement current production. This can happen if suppliers might be short of requirements at present, but will exceed requirements in the future. It enables efficient use of excess production today, or helps to achieve lower transportation costs.

Current practice

Currently, IAS 18 states that when goods or services are exchanged or swapped for goods or services which are of a similar nature and value, the exchange is not regarded as a transaction which generates revenue.

Potential impact of new proposals

The scoping section of the ED states that it will apply to all contracts with customers except (amongst other things):

“... non-monetary exchanges between entities in the same line of business to facilitate sales to customers other than the parties to the exchange (for example, an exchange of oil to fulfil demand on a timely basis in a specified location) ...”

While such parties could technically meet the definition of a customer, for various reasons, the Boards decided to scope these exchanges out.

How we see it

It is our understanding the Boards did not expect the treatment of inventory exchanges to change as a result of the proposed new model. However, we do not believe that this has been made clear in the wording of the ED.

The change in the wording from goods or services that are “similar in nature and value”, to exchanges between entities in the “same line of business”, means that it is unclear whether some transactions that are currently treated as exchanges of dissimilar goods and hence, revenue generating, may now not be considered to be revenue generating because the entities are in the same line of business.

Also, while the scoping section of the ED makes it clear that inventory exchanges do not result in revenue generation, it does not provide guidance on how such transaction should be accounted for. Given the lack of clarity, the divergence in accounting may continue.

Next steps

Mining companies should familiarise themselves, not only with the matters outlined in this publication, but also with the details of the new revenue recognition model. While the comment period in relation to the ED is now closed, the standard is not yet finalised and may differ from the ED.

Therefore, companies should continue to consider the impact the changes may have on their business. They should also continue to discuss these potential changes with the Audit Committee, the Board and their auditors. Furthermore, entities should consider the process for communications with shareholders, analysts and other users.

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Ernst & Young's Global Mining & Metals Center

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